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April 22, 2008

AGENDA ITEM 8a

TO: MEMBERS OF THE HEALTH BENEFITS COMMITTEE

- I. SUBJECT:** Medicare Part D Retiree Drug Subsidy
- II. PROGRAM:** Health Benefits
- III. RECOMMENDATION:** Staff recommends that the Board: (1) Employ a disbursement strategy linked to Retiree Drug Subsidy (RDS) funds actually received and reconciled, (2) Distribute RDS funds to contracting agencies based on each agency's contribution toward its annuitants' health care premiums, (3) Establish a procedure and implement processes between CalPERS, the State Controller's Office and the contracting agencies for the distribution of funds, and (4) Distribute future year funds in the same manner after the required reconciliations.

IV. BACKGROUND:

The Medicare Prescription Drug, Improvement, and Modernization Act established a voluntary Medicare prescription drug benefit program (Part D) effective January 1, 2006. For 2006, 2007, and 2008, the CalPERS Board of Administration voted to participate in Part D by applying for the RDS for Medicare-eligible members not enrolled in the Kaiser Medicare Senior Advantage program, and by providing the Kaiser Medicare Advantage Prescription Drug Plan for Kaiser Senior Advantage enrollees. In addition, CalPERS collected RDS amounts with respect to Part D-eligible members enrolled in the Peace Officers' Research Association of California (PORAC) health benefits plan for calendar years 2006 and 2007. For 2008, PORAC's health benefits plan began operating its own Medicare Prescription Drug Plan and thereby no longer generates RDS amounts. CalPERS is not the sponsor of the California Association of Highway Patrolmen and the California Correctional Peace Officers' Association (CCPOA) health benefits plans. The Department of Personnel Administration, however, directs CalPERS to collect RDS amounts with respect to Part D-eligible members enrolled in CCPOA's health benefits plan.

RDS Funds Received

The Centers for Medicare and Medicaid Services (CMS) uses claims experience for RDS-eligible annuitants to calculate the amount of RDS payments it makes to CalPERS (28 percent of allowable drug costs between specified dollar thresholds per calendar year). Based on contracting agency annuitants' claims experience, CalPERS received \$14 million for 2006 RDS claims, and, approximately \$14 million for 2007 RDS claims. CalPERS and CMS reconciled the 2006 subsidy amounts on March 17, 2008.

Applicable Legislation

Government Code Section 22910, subdivision (f) provides that:

“Amounts received by the board for retiree drug subsidy payments that are attributed to contracting agencies and their annuitants and employees pursuant to subdivision (c) of Section 22910.5 shall be deposited in the Public Employees' Contingency Reserve Fund. Notwithstanding Section 13340, these amounts are continuously appropriated, without regard to fiscal year, for the payment of premiums, costs, contributions, or other benefits related to contracting agencies and their employees and annuitants, and as consistent with the Medicare Prescription Drug Improvement and Modernization Act, as amended.”

Government Code Section 22910, subdivision (g) further provides the Legislature with authority to appropriate funds from the Account for State Government Medicare Drug Subsidies within the Public Employees' Contingency Reserve Fund to, among other things, reduce the contributions the state makes from the General Fund toward health benefits for state annuitants. As a result, the annuitant health benefits' budget line item for 2007-2008 will include RDS funds attributable to the state, less administrative costs and a 5% reserve.

Recommended Approach for Contracting Agencies

Staff recommends that CalPERS treat RDS funds attributable to contracting agencies the same as the state's portion of the RDS funds. Therefore, CalPERS should distribute RDS funds directly to contracting agency employers to reduce agency contributions toward health benefit premiums for their annuitants.

V. ANALYSIS:

RDS Process

CMS makes RDS payments based on eligibility information it receives from CalPERS, and claims information it receives from our health plan partners. Within 15 months of the end of the subsidy period, CalPERS must reconcile its accounts, which may lead to an adjustment in the payment CalPERS is eligible to

receive. This reconciliation process includes validating the covered annuitant information, reporting actual drug costs for the calendar year, adjusting for pharmacy rebates, and calculating the final subsidy amount. CMS compares the final subsidy amount with the interim subsidy payments CalPERS received over the past year, and a difference in those amounts leads to an adjustment in the RDS payment CalPERS is eligible to receive.

In addition, CMS may audit CalPERS submissions and, if the audit determines CMS overpaid CalPERS, CMS will require repayment of the overpaid amount, with an added penalty.

Need for Reserve

At this point in the maturation of the Part D program, it is not possible to determine the outcome of the full CMS review process, including a possible audit. Staff therefore believes it is prudent to maintain a reserve to manage potential reconciliation discrepancies as a result of a CMS audit. Staff recommends employing a disbursement strategy linked to funds actually received and reconciled, as well as retaining a prudent reserve of five percent for Medicare Part D payments.

Reconciliation Schedule

The 2006 plan year reconciliation schedule included the following steps:

- January 11, 2008: CalPERS formally initiates 2006 reconciliation process with CMS
- Jan 22, 2008: CalPERS sends health plans final list of 2006 qualified annuitants
- March 12, 2008: Medstat finalizes the pharmacy personal health information and rebate adjustments and CalPERS completes the coordination of individual retiree costs process.
- March 14, 2008: Health plans submit final 2006 cost data with rebates applied. CalPERS validates RDS cost data and adjustments
- March 17, 2008: CalPERS validation of cost data and adjustments
- March 17, 2008 CalPERS completes 2006 reconciliation (two weeks early)
- March 31, 2008: CMS 2006 Reconciliation Deadline

Funds Available for Distributing to Contracting Agencies

The contracting agency RDS funds available for distribution represent the RDS funds received, less CalPERS administrative costs and the reserve amount. The table below shows the estimated 2006 contracting agency RDS funds available for distribution, assuming the Board chooses to reserve five percent.

Estimated 2006 Contracting Agency RDS Funds Available for Distribution

Category	Amount
2006 contracting agency RDS funds received	\$14,046,628
Less estimated CalPERS annual administrative costs	(\$153,108)
Less 5% reserve	(\$702,331)
Total 2006 contracting agency RDS funds available for distribution	\$13,191,189

Distribution Methods

Staff investigated three methods on which to base the calculation of RDS distribution amounts:

- claims experience
- average spend, and
- employer premium contributions.

Below is a description of each method and an assessment of its viability.

Claims Experience

Under the *claims experience* distribution method, staff would base the amount of RDS funds a contracting agency receives on the actual claims experience of each agency's annuitants. For employers with only one, or a limited number, of RDS-eligible annuitant(s), this would result in identifying the individual(s) who incurred drug costs, which would constitute a violation of the Health Information Portability and Accountability Act. This is not a viable alternative since 100 contracting agencies have only one RDS-eligible annuitant enrolled in a CalPERS health benefits plan. In addition, 452 of our contracting agencies have from 2 to 25 Medicare members, and 77 agencies have from 26 to 50 Medicare members.

Average Spend

Under the *average spend* distribution method, contracting agency employers would receive a set amount for each annuitant, based on the average prescription drug costs for all public agency annuitants. This is not an equitable alternative since this approach might result in a contracting agency receiving a higher reimbursement from the RDS funds than the agency contributed toward premiums for its annuitants.

Employer Premium Contributions

Under the *employer premium contribution* distribution method, CalPERS would provide RDS funds to each contracting agency employer by calculating the following ratio: each contracting agency's health care premium

contribution for its annuitants divided by the total of all contracting agencies' employer health care premium contributions for annuitants. Staff would apply the "contribution ratio" to the total RDS attributable to contracting agencies to calculate each contracting agency's share of the subsidy.

For example, assume that:

- The total of all contracting agency employer health care premium contributions for annuitants is \$400,000 (adjusted for administrative costs and reserve amounts), and
- A contracting agency contributes \$40,000 toward annuitant health care premiums, and
- The RDS funds attributable to contracting agencies is \$100,000.

We would calculate the share for this hypothetical contracting agency as follows:

Contracting Agency Contribution Toward Annuitant Health Care Premiums	Total Amount Contributed Toward Annuitant Health Care Premiums by all Contracting Agencies	Contribution Ratio	RDS Attributed to Contracting Agencies	Contracting Agency Employer Subsidy Share
\$40,000	÷ \$400,000	= 10%	× \$100,000	= \$10,000

This method is a viable alternative because it equitably distributes the funds according to each contracting agency's contribution.

VI. STAFF RECOMMENDATION

Staff recommends that the Board: (1) Employ a disbursement strategy linked to RDS funds actually received and reconciled, (2) Distribute RDS funds to contracting agencies based on each agency's contribution toward its annuitants' health care premiums, (3) Establish a procedure and implement processes between CalPERS, the State Controller's Office and the contracting agencies for the distribution of funds, and (4) Distribute future year funds in the same manner after the required reconciliations.

VII. STRATEGIC PLAN:

This item supports Strategic Plan Goal X, which requires CalPERS to develop and administer quality, sustainable health benefit programs that are responsive to and valued by enrollees and employers.

VII. RESULTS/COSTS:

There are no costs to CalPERS associated with this item. This program is funded through RDS funds.

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